REGIS CORP
Form 10-Q
February 07, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2007

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 1-12725

Regis Corporation
(Exact name of registrant as specified in its charter)

Minnesota	**41-0749934**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
7201 Metro Boulevard, Edina, Minnesota	**55439**
(Address of principal executive offices)	(Zip Code)

(952) 947-7777
(Registrant s telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the Registrant is a shell company (as defined by Rule 12b-2 of the Act). Yes o No x

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of February 5, 2008:

Common Stock, $0.05 par value	**42,884,215**
Class	Number of Shares

REGIS CORPORATION

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PART I - FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Information

REGIS CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEET (Unaudited)
as of December 31, 2007 and June 30, 2007
(In thousands, except per share data)

	December 31, 2007	June 30, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 172,855	$ 184,785
Receivables, net	51,153	67,773
Inventories	208,107	196,582
Deferred income taxes	9,699	18,775
Other current assets	65,346	57,149
Total current assets	507,160	525,064
Property and equipment, net	484,499	494,085
Goodwill	829,446	812,383
Other intangibles, net	191,182	213,452
Investment in affiliates	89,086	20,213
Other assets	82,606	66,917
Total assets	$ 2,183,979	$ 2,132,114
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Long-term debt, current portion	$ 244,041	$ 223,352
Accounts payable	69,573	74,532
Accrued expenses	212,660	240,748
Total current liabilities	526,274	538,632
Long-term debt and capital lease obligations	523,265	485,879
Other noncurrent liabilities	203,646	194,295
Total liabilities	1,253,185	1,218,806
Shareholders equity:		
Common stock, $0.05 par value; issued and outstanding 42,881,965 and 44,164,645 common shares at December 31, 2007 and June 30, 2007, respectively	2,144	2,209
Additional paid-in capital	141,321	178,029
Accumulated other comprehensive income	97,174	78,278
Retained earnings	690,155	654,792
Total shareholders equity	930,794	913,308
Total liabilities and shareholders equity	$ 2,183,979	$ 2,132,114

The accompanying notes are an integral part of the unaudited Condensed Consolidated Financial Information.

REGIS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS (Unaudited)
for the three months ended December 31, 2007 and 2006
(In thousands, except per share data)

	2007	2006
Revenues:		
Service	$ 457,868	$ 440,345
Product	202,696	196,752
Royalties and fees	21,677	19,893
	682,241	656,990
Operating expenses:		
Cost of service	265,977	249,613
Cost of product	105,045	100,164
Site operating expenses	48,844	54,967
General and administrative	86,144	81,411
Rent	99,768	93,163
Depreciation and amortization	31,604	30,412
Total operating expenses	637,382	609,730
Operating income	44,859	47,260
Other income (expense):		
Interest expense	(11,760)	(10,671)
Interest income and other, net	2,092	1,582
Income before income taxes and equity in income of affiliated companies	35,191	38,171
Income taxes	(13,021)	(11,297)
Equity in income of affiliated companies, net of income taxes	386	
Net income	$ 22,556	$ 26,874
Net income per share:		
Basic	$ 0.52	$ 0.60
Diluted	$ 0.51	$ 0.59
Weighted average common and common equivalent shares outstanding:		
Basic	43,369	44,673
Diluted	43,915	45,596
Cash dividends declared per common share	$ 0.04	$ 0.04

The accompanying notes are an integral part of the unaudited Condensed Consolidated Financial Information.

REGIS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS (Unaudited)
for the six months ended December 31, 2007 and 2006
(In thousands, except per share data)

		2007		2006
Revenues:				
Service	$	917,586	$	874,897
Product		389,478		381,677
Royalties and fees		42,702		39,659
		1,349,766		1,296,233
Operating expenses:				
Cost of service		529,037		495,138
Cost of product		199,122		194,393
Site operating expenses		102,529		110,773
General and administrative		172,496		159,364
Rent		197,531		185,335
Depreciation and amortization		63,186		59,954
Total operating expenses		1,263,901		1,204,957
Operating income		85,865		91,276
Other income (expense):				
Interest expense		(22,338)		(20,509)
Interest income and other, net		4,247		2,393
Income before income taxes and equity in income of affiliated companies		67,774		73,160
Income taxes		(24,671)		(23,193)
Equity in income of affiliated companies, net of income taxes		52		
Net income	$	43,155	$	49,967
Net income per share:				
Basic	$	0.99	$	1.11
Diluted	$	0.98	$	1.09
Weighted average common and common equivalent shares outstanding:				
Basic		43,559		44,858
Diluted		44,172		45,847
Cash dividends declared per common share	$	0.08	$	0.08

The accompanying notes are an integral part of the unaudited Condensed Consolidated Financial Information.

REGIS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)
for the six months ended December 31, 2007 and 2006
(In thousands)

	2007	2006
Cash flows from operating activities:		
Net income	$ 43,155	$ 49,967
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	57,271	53,915
Amortization	5,915	6,039
Equity in income of affiliated companies	(52)	-
Deferred income taxes	(1,202)	3,550
Excess tax benefits from stock-based compensation plans	(1,295)	(2,892)
Stock-based compensation	3,303	2,291
Other noncash items affecting earnings	707	1,497
Changes in operating assets and liabilities:		
Receivables	(4,217)	(9,278)
Inventories	(9,686)	(11,141)
Other current assets	(8,062)	(21,935)
Other assets	(2,270)	(3,729)
Accounts payable	(8,572)	14,947
Accrued expenses	2,287	9,975
Other noncurrent liabilities	14,987	8,075
Net cash provided by operating activities	92,269	101,281
Cash flows from investing activities:		
Capital expenditures	(44,399)	(46,281)
Proceeds from sale of assets	16	133
Asset acquisitions, net of cash acquired and certain obligations assumed	(53,297)	(25,343)
Proceeds from loans and investments	10,000	5,250
Disbursements for loans and investments	(22,500)	(20,063)
Cash portion of beauty school assets contributed	(7,254)	
Net investment hedge settlement		(8,897)
Net cash used in investing activities	(117,434)	(95,201)
Cash flows from financing activities:		
Borrowings on revolving credit facilities	4,773,800	3,336,506
Payments on revolving credit facilities	(4,711,600)	(3,287,500)
Proceeds from issuance of long-term debt	50,000	25,000
Repayments of long-term debt and capital lease obligations	(63,612)	(28,889)
Excess tax benefits from stock-based compensation plans	1,295	2,892
Other, primarily decrease in negative book cash balances	(653)	(2,727)
Repurchase of common stock	(49,957)	(37,481)
Proceeds from issuance of common stock	7,372	8,970
Dividends paid	(3,530)	(3,643)
Net cash provided by financing activities	3,115	13,128
Effect of exchange rate changes on cash and cash equivalents	10,120	1,525
(Decrease) increase in cash and cash equivalents	(11,930)	20,733
Cash and cash equivalents:		
Beginning of period	184,785	135,397
End of period	$ 172,855	$ 156,130

The accompanying notes are an integral part of the unaudited Condensed Consolidated Financial Information.

REGIS CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL INFORMATION
(Unaudited)

1. BASIS OF PRESENTATION OF UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL INFORMATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The unaudited interim Condensed Consolidated Financial Information of Regis Corporation (the Company) as of December 31, 2007 and for the three and six months ended December 31, 2007 and 2006, reflect, in the opinion of management, all adjustments necessary to fairly state the consolidated financial position of the Company as of December 31, 2007 and the consolidated results of its operations and its cash flows for the interim periods. Adjustments consist only of normal recurring items, except for any discussed in the notes below. The results of operations and cash flows for any interim period are not necessarily indicative of results of operations and cash flows for the full year.

The Consolidated Balance Sheet data for June 30, 2007 was derived from audited Consolidated Financial Statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America (GAAP). The unaudited interim Condensed Consolidated Financial Information should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended June 30, 2007 and other documents filed or furnished with the Securities and Exchange Commission (SEC) during the current fiscal year.

The unaudited condensed financial information of the Company as of December 31, 2007 and for the three and six month periods ended December 31, 2007 and 2006 included in this Form 10-Q, has been reviewed by PricewaterhouseCoopers LLP, an Independent Registered Public Accounting Firm. Their separate report dated February 7, 2008 appearing herein, states that they did not audit and they do not express an opinion on that unaudited financial information. Accordingly, the degree of reliance on their report on such information should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers LLP is not subject to the liability provisions of Section 11 of the Securities Act of 1933 for their report on the unaudited financial information because that report is not a report or a part of the registration statement prepared or certified by PricewaterhouseCoopers LLP within the meaning of Sections 7 and 11 of the Act.

Inventories:

Inventories consist principally of hair care products held either for use in services or for sale. Cost of product used in salon services is determined by applying estimated gross profit margins to service revenues, which are based on historical factors including product pricing trends and estimated shrinkage. In addition, the estimated gross profit margin is adjusted based on the results of physical inventory counts performed at least semi-annually and the monthly monitoring of factors that could impact the Company s usage rate estimates. These factors include mix of service sales, discounting, and special promotions. Cost of product sold to salon customers is determined based on the weighted average cost of product to the Company, adjusted for an estimated shrinkage factor. Product and service inventories are adjusted based on the results of physical inventory counts performed at least semi-annually.

Stock-Based Employee Compensation:

Stock-based awards are granted under the terms of the 2004 Long Term Incentive Plan (2004 Plan) and the 2000 Stock Option Plan. Additionally, the Company has outstanding stock options under its 1991 Stock Option Plan, although the Plan terminated in 2001. Under these plans, four types of stock-based compensation awards are granted: stock options, equity-based stock appreciation rights (SARS), restricted stock and restricted stock units (RSUs). The stock-based awards, other than the RSUs, expire within ten years from the grant date. The Company utilizes an option-pricing model to estimate the fair value of options at their grant date. Compensation expense for its stock-based compensation awards, other than RSUs, is generally recognized on a straight-line basis over the five-year vesting period. The RSUs cliff vest after five years, and payment of the RSUs is deferred until January 31 of the year following vesting. Awards granted do not contain acceleration of vesting terms for retirement eligible recipients. The Company s primary employee stock-based compensation grant occurs during the fourth fiscal quarter.

Total compensation expense related to share-based compensation plans was $3.3 million and $2.3 million for the six months ended December 31, 2007 and 2006, respectively. A summary of outstanding and exercisable options as of December 31, 2007, and changes during the three and six months ended December 31, 2007 is presented below:

Summary of Options	**Shares (In thousands)**		**Weighted-Average Exercise Price**
Outstanding at July 1, 2007	2,193	$	22.97
Granted			
Exercised	(29)		24.42
Forfeited or expired	(39)		33.02
Outstanding at September 30, 2007	2,125	$	22.65
Granted			
Exercised	(410)		16.24
Forfeited or expired	(14)		35.41
Outstanding at December 31, 2007	1,701	$	24.08
Exercisable at December 31, 2007	1,329	$	20.61

An additional 356,332 shares are expected to vest with a $36.45 weighted average exercise price and a weighted average remaining contractual life of 7.9 years. The total intrinsic value of options exercised during the three and six months ended December 31, 2007 was $6.1 and $6.3 million, respectively, and $6.6 and $11.2 million for the three and six months ended December 31, 2006, respectively.

A summary of the nonvested restricted stock shares, RSUs and SARs outstanding as of December 31, 2007 and changes during the three and six months ended December 31, 2007 is presented below:

	Nonvested			**SARs Outstanding**		
	Restricted Stock Outstanding Shares/Units		**Weighted Average Grant Date Fair Value**	**Shares**		**Weighted Average Exercise Price**
Balance, June 30, 2007	473,700	$	38.36	400,300	$	37.53
Granted						
Vested/Exercised	(301)		36.20			
Forfeited or expired	(11,150)		37.73	(9,950)		38.61
Balance, September 30, 2007	462,249	$	37.83	390,350	$	38.24
Granted						
Vested/Exercised						
Forfeited or expired				(1,500)		39.11
Balance, December 31, 2007	462,249	$	37.83	388,850	$	38.24

The total unrecognized compensation cost related to unvested stock-based compensation arrangements was $21.6 million at December 31, 2007 and the related weighted average period over which it is expected to be recognized is approximately 3.5 years.

Recent Accounting Pronouncements:

In September 2006, the FASB issued Statement of Financial Accounting Standard (SFAS) No. 157, *Fair Value Measures* (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and enhances disclosures about fair value measures required

under other accounting pronouncements, but does not change existing guidance as to whether or not an instrument is carried at fair value. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 (i.e., the Company s first quarter of fiscal year 2009). On November 14, 2007, the FASB proposed deferral of SFAS No. 157 s effective date for all non-financial assets and liabilities, except those items recognized or disclosed at fair value on an annual or more frequently recurring basis, until years beginning after November 15, 2008. The Company is currently evaluating the impact of SFAS No. 157 on its Consolidated Financial Statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159). SFAS No. 159 permits companies to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. Companies are not allowed to adopt SFAS No. 159 on a retrospective basis unless they choose early adoption. If the Company chooses to adopt SFAS No. 159, the Company will adopt at the beginning of fiscal year 2009. The Company is currently evaluating the impact of SFAS No. 159 on its Consolidated Financial Statements.

In September 2006, the Emerging Issues Task Force (EITF) ratified Issue No. 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. EITF No. 06-4 addresses whether or not an employer needs to recognize a liability for future benefits based on the agreement with the employee under the endorsement split-dollar life insurance arrangement. It focuses exclusively on endorsement split-dollar life insurance arrangements that provide a benefit to an employee that extends to postretirement periods. The Issue does not apply to a split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee s active service period with an employer. The EITF will be effective for fiscal years beginning after December 15, 2007 (i.e., fiscal year 2009). The Company is currently evaluating the impact of EITF No. 06-4 on its Consolidated Financial Statements and does not expect its application to have a material impact on the Company s Consolidated Financial Statements.

In December 2007, the FASB issued Statement of Financial Accounting Standard No. 141(R), *Business Combinations* (SFAS No. 141(R)). SFAS No. 141(R) changes the accounting for business combinations in a number of areas including the treatment of contingent consideration, preacquisition contingencies, transactions costs, in-process research and development, and restructuring costs. SFAS No. 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company is required to adopt SFAS No. 141(R) at the beginning of fiscal year 2010. The Company is currently evaluating the impact of SFAS No. 141(R) on its Consolidated Financial Statements.

2. SHAREHOLDERS EQUITY AND COMPREHENSIVE INCOME:

Additional Paid-In Capital

The decrease in additional paid-in capital during the six months ended December 31, 2007 was due to the following:

		(Dollars in thousands)
Balance, June 30, 2007	$	178,029
Exercise of stock options		7,351
Franchise stock incentive plan		416
Tax benefit realized upon exercise of stock options		2,330
Stock-based compensation		3,303
FIN 48 adjustment		(237)
Stock repurchase		(49,871)
Balance, December 31, 2007	$	141,321

Comprehensive Income

Components of comprehensive income for the Company include net income, changes in fair market value of financial instruments designated as hedges of interest rate or foreign currency exposure and foreign currency translation charged or credited to the cumulative translation account within shareholders equity. Comprehensive income for the three and six months ended December 31, 2007 and 2006 was as follows:

For the Periods Ended December 31,

	Three Months		Six Months	
	2007	2006	2007	2006
	(Dollars in thousands)			
Net income	$ 22,556	$ 26,874	$ 43,155	$ 49,967
Other comprehensive income (loss):				
Changes in fair market value of financial instruments designated as cash flow hedges of interest rate exposure, net of taxes	(1,101)	359	(2,841)	(687)
Change in cumulative foreign currency translation, net of taxes	9,543	3,141	21,737	7,409
Total comprehensive income	$ 30,998	$ 30,374	$ 62,051	$ 56,689

3. NET INCOME PER SHARE:

The following table sets forth a reconciliation of shares used in the computation of basic and diluted earnings per share:

	For the Periods Ended December 31,			
	Three Months		Six Months	
	2007	2006	2007	2006
	(Shares in thousands)			
Weighted average shares for basic earnings per share	43,369	44,673	43,559	44,858
Effect of dilutive securities:				
Dilutive effect of stock-based compensation	442	872	509	938
Contingent shares issuable under contingent stock agreements (see Note 5).	104	51	104	51
Weighted average shares for diluted earnings per share	43,915	45,596	44,172	45,847
Anti-dilutive stock-based compensation shares excluded from the above computations:				
Stock options, SARs, restricted stock and RSUs	1,209	603	1,193	622

Restricted stock awards, including restricted stock units, of 462,249 shares for the three and six months ended December 31, 2007, and 186,750 shares for the three and six months ended December 31, 2006, were excluded from the computation of basic weighted average shares outstanding as such shares were not yet vested at these dates.

4. GOODWILL AND OTHER INTANGIBLES:

The tables below contain detail related to the Company s recorded goodwill as of December 31, 2007 and June 30, 2007.

	Salons		Beauty	Hair Restoration	
	North America	International	Schools(1)	Centers	Consolidated
			(Dollars in thousands)		
Balance at June 30, 2007	$ 570,161	$ 46,487	$ 60,934	$ 134,801	$ 812,383
Goodwill acquired	20,524	6,039		15,073	41,636
Impact of contribution of certain beauty schools(1)	13,829	13,071	(60,960)		(34,060)
Adjustment related to FIN 48				3,859	3,859
Translation rate adjustments	3,860	1,742	26		5,628
Balance at December 31, 2007	$ 608,374	$ 67,339	$	$ 153,733	$ 829,446

(1) On August 1, 2007, the Company contributed its accredited cosmetology schools to Empire Education Group, Inc. The Company retained ownership of its one North America and four United Kingdom Vidal Sassoon schools. Subsequent to August 1, 2007 results of operations and assets for the Vidal Sassoon schools are included in the respective North American and international salon segments.

Goodwill acquired includes adjustments to prior year acquisitions, including the finalization of purchase price allocations.

Goodwill is tested for impairment annually or at the time of a triggering event in accordance with the provisions of SFAS No. 142, *Goodwill and Other Intangible Assets*. Fair values are estimated based on the Company s best estimate of the expected present value of future cash flows and compared with the corresponding carrying value of the reporting unit, including goodwill. Where available and as appropriate, comparative market multiples are used to corroborate the results of the present value method. The Company considers its various concepts to be reporting units when it tests for goodwill impairment because that is where the Company believes goodwill resides. The Company s policy is to perform

its annual goodwill impairment test during its fiscal third quarter of each fiscal year ending June 30.

Related to FIN 48 the Company recorded a $3.9 million adjustment to goodwill to account for preacquisition tax positions at the Company s hair restoration centers segment.

The table below presents other intangible assets as of December 31, 2007 and June 30, 2007:

	December 31, 2007			June 30, 2007		
	Cost	Accumulated Amortization (1)	Net	Cost	Accumulated Amortization (1)	Net
	(Dollars in thousands)					
Amortized intangible assets:						
Brand assets and trade names	$ 110,987	$ (11,485)	$ 99,502	$ 112,999	$ (10,193)	$ 102,806
Customer lists	51,317	(14,845)	36,472	48,744	(9,970)	38,774
Franchise agreements	33,012	(8,680)	24,332	27,149	(7,538)	19,611
Product license agreements	18,523	(3,524)	14,999	16,946	(2,944)	14,002
School-related licenses				25,428	(1,247)	24,181
Non-compete agreements	739	(614)	125	691	(644)	47
Other	21,741	(5,989)	15,752	21,661	(7,630)	14,031
	$ 236,319	$ (45,137)	$ 191,182	$ 253,618	$ (40,166)	$ 213,452

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(1) Balance sheet accounts are converted at the applicable exchange rates effective as of the reported balance sheet dates, while income statement accounts are converted at the average exchange rates for the year-to-date periods presented.

All intangible assets have been assigned an estimated finite useful life and are amortized over the number of years that approximate their respective useful lives (ranging from one to 40 years). The cost of intangible assets is amortized to earnings in proportion to the amount of economic benefits obtained by the Company in that reporting period. The weighted average amortization periods, in total and by major intangible asset class, are as follows:

	Weighted Average Amortization Period (In years)
Amortized intangible assets:	
Brand assets and trade names	39
Customer lists	10
Franchise agreements	21
Product license agreements	30
Non-compete agreements	6
Other	19
Total	28

Total amortization expense related to amortizable intangible assets was approximately $2.9 million during the three months ended December 31, 2007 and 2006, and $5.8 million during the six months ended December 31, 2007 and 2006. As of December 31, 2007, future estimated amortization expense related to amortizable intangible assets is estimated to be:

Fiscal Year		**(Dollars in thousands)**
2008 (Remainder: six-month period)	$	6,008
2009		12,348
2010		12,086
2011		11,876
2012		11,659

5. ACQUISITIONS, LOANS AND INVESTMENTS:

Acquisitions

During the six months ended December 31, 2007 and 2006, the Company made numerous salon and hair restoration center acquisitions and the purchase prices have been allocated to assets acquired and liabilities assumed based on their estimated fair values at the dates of acquisition. Operations of the acquired companies have been included in the operations of the Company since the date of the respective acquisition.

The components of the aggregate purchase prices of the acquisitions made during the six months ended December 31, 2007 and 2006 and the allocation of the purchase prices were as follows:

Allocation of Purchase Prices	For the Six Months Ended December 31, 2007	2006
	(Dollars in thousands)	
Components of aggregate purchase prices:		
Cash	$ 53,297	$ 25,343
Liabilities assumed	2,602	844
	$ 55,899	$ 26,187
Allocation of the purchase price:		
Current assets	$ 2,022	$ 1,964
Property and equipment	5,664	3,774
Deferred income tax asset		1,043
Other noncurrent assets	1,210	9
Goodwill	41,636	17,873
Identifiable intangible assets	7,978	2,044
Accounts payable and accrued expenses	(2,611)	(84)
Deferred income tax liability		(436)
	$ 55,899	$ 26,187

In a limited number of acquisitions, the Company guarantees that the stock issued in conjunction with the acquisition will reach a certain market price. If the stock should not reach this price during an agreed upon time frame (typically three years from the date of acquisition), the Company is obligated to issue additional consideration to the sellers. Once the agreed upon stock price is met or exceeded for a period of five consecutive days, the contingency is met and the Company is no longer liable. At December 31, 2007, one contingency of this type exists, which expires in March of 2008. Based on the December 31, 2007 market price, the Company would be required to provide an additional 103,650 shares with an aggregate market value on that date of $2.9 million related to this acquisition contingency if the agreed upon time frame was assumed to have expired December 31, 2007. These contingently issuable shares have been included in the calculation of diluted earnings per share.

The majority of the purchase price in salon acquisitions is accounted for as residual goodwill rather than identifiable intangible assets. This stems from the value associated with the walk-in customer base of the acquired salons, which is not recorded as an identifiable intangible asset under current accounting guidance, as well as the limited value and customer preference associated with the acquired hair salon brand. Key factors considered by consumers of hair salon services include personal relationships with individual stylists, service quality and price point competitiveness. These attributes represent the going concern value of the salon.

Residual goodwill further represents the Company s opportunity to strategically combine the acquired business with the Company s existing structure to serve a greater number of customers through its expansion strategies. In the acquisitions of international salons and hair restoration centers, the residual goodwill primarily represents the growth prospects that are not captured as part of acquired tangible or identified intangible assets. Generally, the goodwill recognized in the North American salon transactions is expected to be fully deductible for tax purposes and the goodwill recognized in the international salon transactions is non-deductible for tax purposes. Goodwill generated in certain acquisitions, such as Hair Club, is not deductible for tax purposes due to the acquisition structure of the transaction.

During the six months ended December 31, 2007 and 2006, the Company purchased certain salon operations from its franchisees. The Company evaluated the effective settlement of the preexisting franchise contracts and associated rights afforded by those contracts in accordance with Emerging Issues Task Force (EITF) No. 04-1, *Accounting for Preexisting Relationships Between the Parties to a Business Combination.* The Company determined that the effective settlement of the preexisting franchise contracts at the date of the acquisition did not result in a gain or loss, as the agreements were neither favorable nor unfavorable when compared to similar current market transactions, and no settlement provisions exist in the preexisting contracts. Therefore, no settlement gain or loss was recognized with respect to the Company s franchise buybacks.

Loans and Investments

On August 1, 2007, the Company contributed its 51 wholly-owned accredited cosmetology schools to Empire Education Group, Inc., in exchange for a 49.0 percent minority interest in Empire Education Group, Inc. The carrying value of the contributed schools approximated the estimated fair value of the Company s interest in Empire Education Group, Inc., resulting in no gain or loss on the date of contribution. The Company s investment in Empire Education Group, Inc. is accounted for under the equity method of accounting. Subsequent to August 1, 2007, the Company completed $22.5 million of loans and advances to Empire Education Group, Inc., of which $12.5 million was outstanding at December 31, 2007. The Company recorded $0.4 million of interest income related to these loans and advances during the six months ended December 31, 2007. During the six months ended December 31, 2007, the Company recorded $0.7 million of equity earnings related to its investment in Empire Education Group, Inc. In January 2008, the Company s effective ownership interest increased to 55.1 percent related to the buyout of Empire s minority interest shareholder. In connection with the buyout, the Company advanced Empire Education Group, Inc., an additional $21.4 million. The Company will continue to account for the investment in Empire Education Group, Inc., under the equity method of accounting as Empire retains majority voting interest.

The Company holds exchangeable notes issued by Yamano Holding Corporation and a loan obligation of a Yamano Holdings subsidiary, Beauty Plaza Co. Ltd., for an aggregate amount of $11.0 million. A portion of the notes are exchangeable for approximately 14.8 percent of the outstanding shares of Beauty Takashi Co. Ltd., a subsidiary of Yamano Holdings. The exchangeable portion of the notes is accounted for as a cost method investment. The Company recorded less than $0.1 million in income related to the exchangeable notes and loan obligation during the six months ended December 31, 2007. In connection with the purchase of the exchangeable notes and loan obligation, the parties also entered into a business collaboration agreement with respect to their joint pursuit of opportunities relating to retail hair salons in Asia.

The Company holds a 50.0 percent interest in Intelligent Nutrients, LLC. The Company is accounting for this investment under the equity method. Intelligent Nutrients, LLC currently carries a wide variety of organic, harmonically grown products, including dietary supplements, coffees, teas and aromatics. Additionally, a full line of professional hair care and personal care products is in development and is expected to be available in the spring of calendar year 2008. These products will be offered at the Company s corporate and franchise salons, and eventually in other independently owned salons. During the six months ended December 31, 2007 the Company recorded a loss of $0.9 million net of $0.4 million of tax benefit related to this equity investment.

The Company holds a 19.9 percent interest in the voting common stock of Cameron Capital I, Inc. (CCI). CCI owns and operates PureBeauty and BeautyFirst salons. The investment is accounted for under the equity method. As of December 31, 2007 and June 30, 2007 the Company also had $10.0 million of long-term notes receivable under a credit agreement with the majority corporate investor in this privately held entity. During the six months ended December 31, 2007, the Company recorded a loss of less than $0.1 million related to this equity investment. See Note 10 for subsequent event related to this investment.

The Company holds an interest of less than 20 percent in the preferred stock of a privately held entity, Cool Cuts 4 Kids, Inc. This investment is accounted for under the cost method. During fiscal year 2006, the Company determined that its investment was impaired and recognized an impairment loss within interest income and other, net in the Consolidated Statement of Operations for the full carrying value. The Company s securities purchase agreement contains a call provision, giving the Company the right of first refusal should the privately held entity receive a bona fide offer from another company, as well as the right to purchase all of the assets of the privately held entity during the period from April 1, 2008 to January 31, 2009 for a multiple of cash flow.

6. LITIGATION:

The Company is a defendant in various lawsuits and claims arising out of the normal course of business. Like certain other large retail employers, the Company has been faced with allegations of purported class-wide wage and hour violations. Litigation is inherently unpredictable and the outcome of these matters cannot presently be determined. Although company counsel believes that the Company has valid defenses in these matters, it could in the future incur judgments or enter into settlements of claims that could have a material adverse effect on its results of operations in any particular period.

7. DERIVATIVE FINANCIAL INSTRUMENTS:

The primary market risk exposure of the Company relates to changes in interest rates in connection with its debt, some of which bears interest at variable rates based on LIBOR plus an applicable borrowing margin. Additionally, the Company is exposed to foreign currency translation risk related to its net investments in its foreign subsidiaries and, to a lesser extent, foreign currency denominated transactions. The Company has established policies and procedures that govern the management of these exposures through the use of derivative financial instrument contracts. By policy, the Company does not enter into such contracts for the purpose of speculation.

In September 2007 the Company entered into several forward foreign currency contracts to hedge the U.S. Dollar value of future Chinese Yuan denominated payments to Chinese vendors. The foreign currency contracts totaled approximately 6.0 million Chinese Yuan or $0.8 million U.S. dollars and have maturation dates between April 2008 and September 2008. The purpose of the forward contracts is to protect against adverse movements in the Chinese Yuan exchange rate. The contracts were designated and are effective as cash flow hedges of Chinese Yuan denominated foreign currency firm commitments. These cash flow hedges were recorded at fair value within other current assets in the Condensed Consolidated Balance Sheet, with a corresponding offset in other comprehensive income within shareholders equity.

8. INCOME TAXES:

The reported effective tax rate was 37.0 percent and 29.6 percent for the three months ended December 31, 2007 and 2006, respectively, and 36.4 percent and 31.7 percent for the six months ended December 31, 2007 and 2006, respectively. The provision for income taxes differs from the amount of income tax determined by applying the applicable United States (U.S.) statutory rate to earnings before income taxes, as a result of the following:

	For the Periods Ended December 31,			
	Three Months		Six Months	
Tax Rate Reconciliation	**2007**	**2006**	**2007**	**2006**
U.S. statutory tax rate	35.0%	35.0%	35.0%	35.0%
Adjustments resulting from:				
State income taxes, net of federal income tax benefit	4.3	2.2	4.0	2.5
Foreign income taxes at other than U.S. rates	(3.0)	(2.7)	(2.9)	(2.7)
Work Opportunity Tax Credits and jobs tax credits, net	(2.1)	(6.8)	(1.8)	(3.4)
Other, net	2.8	1.9	2.1	0.3
Effective income tax rate	37.0%	29.6%	36.4%	31.7%

The Company adopted the provisions of FIN 48 effective July 1, 2007. As a result of adoption, the Company recognized a $20.7 million increase in the liability for unrecognized income tax benefits, including interest and penalties, which was accounted for through the following accounts (dollars in thousands):

Deferred income taxes	$	10,128
Goodwill		6,094
Additional paid-in capital		237

Retained earnings		4,201
Total increase	$	20,660

On July 1, 2007, the Company had gross unrecognized tax benefits of $22.5 million, of which $6.5 million would affect the effective tax rate if recognized.

The Company recognizes accrued interest and penalties related to unrecognized tax benefits as a component of income tax expense in its financial statements. As of the adoption date, the Company had accrued interest and penalties related to unrecognized tax benefits of $7.2 million. This amount is not included in the gross unrecognized tax benefits noted above.

The Company files tax returns and pays tax primarily in the United States, Canada, the United Kingdom, and a number of countries in continental Europe as well as states, cities, and provinces within these jurisdictions. With few exceptions,

tax years prior to June 30, 2004 are closed to audit. The Company, or its subsidiaries, is currently under audit by a number of states as well as Canada and the United Kingdom, and it is reasonably certain that some or all of these audits might be resolved within the next twelve months. Resolution of these audits could result in offsets to other balance sheet accounts, cash payments, and/or adjustments to the annual effective rate. The Company does not expect a significant increase or decrease in unrecognized tax benefits over the next 12 months. Between July 1, 2007 and December 31 2007, there were no material changes to the Company s gross liability for unrecognized tax benefits.

9. SEGMENT INFORMATION:

As of December 31, 2007, the company owned, franchised or held ownership interests in over 12,600 worldwide locations. The Company s locations consisted of 9,967 North American salons (located in the United States, Canada and Puerto Rico), 2,103 international salons, 90 hair restoration centers and approximately 475 locations in which the Company maintains an ownership interest. The Company operates its North American salon operations through five primary concepts: Regis Salons, MasterCuts, Trade Secret, SmartStyle and Strip Center salons. The concepts offer similar products and services, concentrate on the mass market consumer marketplace and have consistent distribution channels. All of the company-owned and franchise salons within the North American salon concepts are located in high traffic, retail shopping locations that attract mass market consumers, and the individual salons generally display similar economic characteristics. The salons share interdependencies and a common support base. The Company s international salon operations, which are primarily in Europe, are located in malls, leading department stores, mass merchants and high-street locations. The Company s hair restoration centers are located in the United States and Canada.

On August 1, 2007, the Company contributed its accredited cosmetology schools to Empire Education Group, Inc. The results of operations for the month ended July 31, 2007 for the accredited cosmetology schools are reported in the North American salons segment. The Company retained ownership of its one North America and four United Kingdom Vidal Sassoon schools. Subsequent to August 1, 2007 results of operations for the Vidal Sassoon schools are included in the respective North American and international salon segments.

Based on the way the Company manages its business, it has reported its North American salons, international salons and hair restoration centers as three separate reportable operating segments.

Financial information for the Company s reporting segments is shown in the following tables:

Assets by Segment	**December 31, 2007**	**June 30, 2007**
	(Dollars in thousands)	
North American salons	$ 1,261,605	$ 1,070,776
International salons	251,969	210,629
Beauty schools		163,818
Hair restoration centers	277,480	262,295
Unallocated corporate	392,925	424,596
Consolidated	$ 2,183,979	$ 2,132,114

	For the Three Months Ended December 31, 2007(1)				
	Salons		Hair Restoration Centers	Unallocated Corporate	Consolidated
	North America	International			
	(Dollars in thousands)				
Revenues:					
Service	$ 399,377	$ 43,224	$ 15,267	$	$ 457,868
Product	166,803	19,133	16,760		202,696
Royalties and fees	9,900	10,699	1,078		21,677
	576,080	73,056	33,105		682,241
Operating expenses:					
Cost of service	233,667	24,091	8,219		265,977
Cost of product	90,002	10,117	4,926		105,045
Site operating expenses	43,829	3,708	1,307		48,844
General and administrative	33,394	11,786	7,357	33,607	86,144
Rent	83,324	14,284	1,728	432	99,768
Depreciation and amortization	21,690	2,589	2,552	4,773	31,604
Total operating expenses	505,906	66,575	26,089	38,812	637,382
Operating income (loss)	70,174	6,481	7,016	(38,812)	44,859
Other income (expense):					
Interest				(11,760)	(11,760)
Other, net				2,092	2,092
Income (loss) before income taxes and equity in income of affiliated companies	$ 70,174	$ 6,481	$ 7,016	$ (48,480)	$ 35,191

(1) On August 1, 2007, the Company contributed its accredited cosmetology schools to Empire Education Group, Inc. The Company retained ownership of its one North America and four United Kingdom Vidal Sassoon schools. Results of operations for the Vidal Sassoon schools are included in the respective North American and international salon segments.

	For the Three Months Ended December 31, 2006					
	Salons			Hair		
	North America	International	Beauty Schools	Restoration Centers	Unallocated Corporate	Consolidated
	(Dollars in thousands)					
Revenues:						
Service	$ 372,161	$ 35,234	$ 20,142	$ 12,808	$	$ 440,345
Product	163,256	15,919	1,834	15,743		196,752
Royalties and fees	9,496	9,216		1,181		19,893
	544,913	60,369	21,976	29,732		656,990
Operating expenses:						
Cost of service	215,863	18,618	8,184	6,948		249,613
Cost of product	84,591	9,883	1,126	4,564		100,164
Site operating expenses	46,739	2,721	4,216	1,291		54,967
General and administrative	30,345	11,556	2,796	6,542	30,172	81,411
Rent	77,690	11,111	2,241	1,608	513	93,163
Depreciation and amortization	20,631	2,193	829	2,390	4,369	30,412
Total operating expenses	475,859	56,082	19,392	23,343	35,054	609,730
Operating income (loss)	69,054	4,287	2,584	6,389	(35,054)	47,260
Other income (expense):						
Interest					(10,671)	(10,671)
Other, net					1,582	1,582
Income (loss) before income taxes	$ 69,054	$ 4,287	$ 2,584	$ 6,389	$ (44,143)	$ 38,171

	For the Six Months Ended December 31, 2007(1)				
	Salons		Hair		
	North America	International	Restoration Centers	Unallocated Corporate	Consolidated
	(Dollars in thousands)				
Revenues:					
Service	$ 806,516	$ 81,653	$ 29,417	$	$ 917,586
Product	321,636	34,426	33,416		389,478
Royalties and fees	20,049	20,258	2,395		42,702
	1,148,201	136,337	65,228		1,349,766
Operating expenses:					
Cost of service	468,555	44,512	15,970		529,037
Cost of product	170,635	18,728	9,759		199,122
Site operating expenses	93,037	6,915	2,577		102,529
General and administrative	66,388	23,600	14,516	67,992	172,496
Rent	166,320	26,913	3,385	913	197,531
Depreciation and amortization	43,585	5,048	5,049	9,504	63,186
Total operating expenses	1,008,520	125,716	51,256	78,409	1,263,901
Operating income (loss)	139,681	10,621	13,972	(78,409)	85,865
Other income (expense):					
Interest				(22,338)	(22,338)
Other, net				4,247	4,247
Income (loss) before income taxes and equity in income of affiliated companies	$ 139,681	$ 10,621	$ 13,972	$ (96,500)	$ 67,774

(1) On August 1, 2007, the Company contributed its accredited cosmetology schools to Empire Education Group, Inc. For the six months ended December 31, 2007, the results of operations for the month ended July 31, 2007 for the accredited cosmetology schools are reported in the North American salons segment. The Company retained ownership of its one North America and four United Kingdom Vidal Sassoon schools. Subsequent to August 1, 2007 results of operations for the Vidal Sassoon schools are included in the respective North American and international salon segments.

	For the Six Months Ended December 31, 2006					
	Salons			Hair		
			Beauty	Restoration	Unallocated	
	North America	International	Schools	Centers	Corporate	Consolidated
	(Dollars in thousands)					
Revenues:						
Service	$ 743,360	$ 68,924	$ 37,106	$ 25,507	$	$ 874,897
Product	317,164	29,360	4,235	30,918		381,677
Royalties and fees	19,295	17,960		2,404		39,659
	1,079,819	116,244	41,341	58,829		1,296,233
Operating expenses:						
Cost of service	428,235	36,596	16,220	14,087		495,138
Cost of product	164,295	17,875	2,928	9,295		